

# **CITY OF FAITH**

## **NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2013**

### **(1) Summary of Significant Accounting Policies**

As discussed further in Note (1)c, these financial statements are presented on a modified cash basis of accounting. The modified cash basis of accounting differs from accounting principles generally accepted in the United States of America (GAAP). GAAP includes all relevant Governmental Accounting Standards Board (GASB) pronouncements.

#### **a. Reporting Entity**

The reporting entity of the City of Faith (the City) consists of the primary government (which includes all of the funds, organizations, institutions, agencies, departments, and offices that make up the legal entity, plus those funds for which the primary government has a fiduciary responsibility, even though those fiduciary funds may represent organizations that do not meet the criteria for inclusion in the financial reporting entity); those organizations for which the primary government is financially accountable; and other organizations for which the nature and significance of their relationship with the primary government are such that their exclusion would cause the financial reporting entity's financial statements to be misleading or incomplete.

#### **b. Basis of Presentation**

##### Government-wide Financial Statements:

The Statement of Net Position – Modified Cash Basis and Statement of Activities – Modified Cash Basis display information about the reporting entity as a whole. They include all funds of the reporting entity. The statements distinguish between governmental and business-type activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other non-exchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods or services.

The Statement of Activities – Modified Cash Basis presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the City and for each function of the City's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Program revenues include (a) charges paid by recipients of goods and services offered by the programs and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

##### Fund Financial Statements:

Fund financial statements of the reporting entity are organized into funds, each of which is considered to be a separate accounting entity. Each fund is accounted for by providing a separate set of self-balancing accounts that constitute its assets, liabilities, fund equity, revenues, and expenditures/expenses. Funds are organized into two major categories: governmental and proprietary. An emphasis is placed on major funds within the governmental and proprietary categories.

A fund is considered major if it is the primary operating fund of the City or it meets the following criteria:

1. Total assets, liabilities, revenues, or expenditures/expenses of the individual governmental or enterprise fund are at least ten percent of the corresponding total for all funds of that category or type, and
2. Total assets, liabilities, revenues, or expenditures/expenses of the individual governmental or enterprise fund are at least five percent of the corresponding total for all governmental and enterprise funds combined, or
3. Management has elected to classify one or more governmental or enterprise funds as major for consistency in reporting from year to year, or because of public interest in the fund's operations.

**CITY OF FAITH**

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2013**

**(1) Summary of Significant Accounting Policies (Continued)**

**b. Basis of Presentation (Continued)**

Fund Financial Statements: (Continued)

The funds of the City financial reporting entity are described below:

Governmental Funds:

General Fund – the general fund is the general operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund. The general fund is always considered to be a major fund.

Proprietary Funds:

Enterprise Funds – enterprise funds are used to account for operations (a) that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

Proprietary Funds include:

██████████ Fund – financed primarily by the sale of ██████████ this fund accounts for construction and operation of the ██████████ store. This is a major fund.

██████████ Fund – financed primarily by user charges; this fund accounts for the construction and operation of the ██████████ system and related facilities (SDCL 9-47-1). This is a major fund.

██████████ Fund – financed primarily by user charges; this fund accounts for the construction and operation of the ██████████ system and related facilities. This is a major fund.

██████████ Fund – financed primarily by user charges; this fund accounts for the construction and operation of the ██████████ system and related facilities (SDCL 9-48-2). This is a major fund.

Telephone Fund – financed primarily by user charges; this fund accounts for the construction and operation of the City telephone system and related facilities. This is a major fund.

██████████ Fund – financed primarily by user charges; this fund accounts for the construction and operation of the ██████████ and ██████████ and ██████████ This is a major fund.

**c. Measurement Focus and Basis of Accounting**

Measurement focus is a term used to describe how transactions are recorded within the various financial statements. Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements, regardless of the measurement focus.

**CITY OF FAITH**

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2013**

**(1) Summary of Significant Accounting Policies (Continued)**

**c. Measurement Focus and Basis of Accounting (Continued)**

*Measurement Focus:*

Government-wide Financial Statements:

In the government-wide Statement of Net Position and Statement of Activities, both governmental and business-type activities are presented using the economic resources measurement focus, applied within the limitations of the modified cash basis of accounting as defined below.

Fund Financial Statements:

In the fund financial statements, the current financial resources measurement focus or the economic resources measurement focus is used, applied within the limitations of the modified cash basis of accounting.

*Basis of Accounting:*

All financial statements are presented using the modified cash basis of accounting. The modified cash basis of accounting involves the measurement of cash and cash equivalents and changes in cash and cash equivalents resulting from cash receipt and disbursement transactions. Under the cash basis of accounting, the statement of financial position reports only cash and cash equivalents. Under the modified cash basis of accounting, transactions are recorded in the accounts when cash and/or cash equivalents are received or disbursed and assets and liabilities are recognized to the extent that cash has been received or disbursed.

Acceptable modifications to the cash basis of accounting implemented by the City in these financial statements are:

1. Recording of capital assets arising from cash transactions and depreciating those assets where appropriate.
2. Recording of long-term debt arising from cash transactions.
3. Recording both capital assets and related long-term debt used to finance the capital asset acquisition.
4. Recording inventory resulting from payment of cash to vendors.
5. Recording of investments arising from cash transactions.
6. Recording of customer's deposits arising from cash transactions.
7. Recording checks returned as non-sufficient funds as accounts receivable.

As a result of the use of the modified cash basis of accounting, certain assets and their related revenues (such as accounts receivable and revenue for billed or provided services not yet collected) and certain liabilities and their related expenses (such as accounts payable and expenses for goods or services received but not yet paid, and accrued expenses and liabilities) are not recorded in these financial statements.

If the City applied GAAP, the fund financial statements for governmental funds would use the modified accrual basis of accounting, while the government-wide financial statements and fund financial statements for proprietary fund types would use the accrual basis of accounting.



**CITY OF FAITH**

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2013**

**(1) Summary of Significant Accounting Policies (Continued)**

**d. Interfund Transfers**

The City transfers unrestricted revenues collected in the enterprise funds to the General Fund and other enterprise funds to balance the budgets in those funds.

**e. Capital Assets**

Under the modified cash basis of accounting, capital assets are recorded when they result from cash transactions, and are depreciated, when appropriate. The accounting treatment for property, plant, and equipment (capital assets) depends on whether the assets are used in governmental fund operations or proprietary fund operations and whether they are reported in the government-wide or fund financial statements.

Government-wide Financial Statements:

Under the modified cash basis of accounting, capital assets are considered a cost of the program for which they were acquired, for the amount paid in cash.

Allocations between programs are made, where necessary, to match the cost with the program that benefits from the use of the capital assets.

All capital assets are valued at cost or estimated historical cost, if actual historical cost is not available.

Infrastructure assets used in general government operations, consisting of certain improvements other than buildings, including roads, bridges, sidewalks, drainage systems, and lighting systems, acquired prior to January 1, 2004, were not required to be capitalized by the City. Infrastructure assets acquired since January 1, 2004, are recorded at cost, and classified as "Improvements Other than Buildings."

Under the modified cash basis, depreciation of all exhaustible capital assets arising from cash transactions is recorded as an allocated expense in the Statement of Activities – Modified Cash Basis, with accumulated depreciation reflected in the Statement of Net Position – Modified Cash Basis. Depreciation has been provided over the estimated useful lives using the straight-line method.

Capitalization thresholds (the dollar values above which asset acquisitions are added to the capital asset accounts), depreciation methods, and estimated useful lives of capital assets reported in the government-wide statements and proprietary funds are as follows:

	<u>Capitalization Threshold</u>	<u>Depreciation Method</u>	<u>Estimated Useful Life</u>
Land	\$ █	██████████	██████████
Construction Work in Progress	\$ █	██████████	██████████
Buildings	\$ █	██████████	██████████
Improvements Other Than Buildings	\$ █	██████████	██████████
Machinery and Equipment	\$ █	██████████	██████████

Land is an inexhaustible capital asset and is not depreciated.

**CITY OF FAITH**

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2013**

**(1) Summary of Significant Accounting Policies (Continued)**

**e. Capital Assets (Continued)**

Fund Financial Statements:

In the fund financial statements, capital assets arising from cash transactions acquired for use in governmental fund operations are accounted for as capital outlay expenditures of the governmental fund when paid for in cash. Capital assets acquired for use in proprietary fund operations are accounted for in the same manner as in the government-wide financial statements.

**f. Long-Term Liabilities**

The accounting treatment of long-term liabilities depends on whether the assets are used in governmental fund operations or proprietary fund operations and whether they are reported in the government-wide or fund financial statements.

All long-term liabilities, arising from cash transactions, to be repaid from governmental and business-type resources are reported as liabilities in the respective columns on the government-wide financial statements. The long-term liability consists of a capital acquisition lease.

Long-term liabilities arising from cash transactions of governmental funds are not reported as liabilities in the fund financial statements. Instead, the debt proceeds are reported as other financing sources and payments of principal and interest are reported as expenditures. The accounting for long-term debt of the proprietary fund is the same in the fund financial statements as it is in the government-wide financial statements.

**g. Revenue Received in Advance**

Under the modified cash basis of accounting, cash may have been received in advance of the City's providing a good or service to a customer, resulting in unearned revenue. There was no unearned revenue at December 31, 2013.

**h. Program Revenues**

Program revenues derive directly from the program itself or from parties other than the City's taxpayers or citizenry, as a whole. Program revenues are classified into three categories, as follows:

1. Charges for services – These arise from charges to customers, applicants, or others who purchase, use, or directly benefit from the goods, services, or privileges provided, or are otherwise directly affected by the services.
2. Program-specific operating grants and contributions – These arise from mandatory and voluntary non-exchange transactions with other governments, organizations, or individuals that are restricted for use in a particular program.
3. Program-specific capital grants and contributions – These arise from mandatory and voluntary non-exchange transactions with other governments, organizations, or individuals that are restricted for the acquisition of capital assets for use in a particular program.

**CITY OF FAITH**

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2013**

**(1) Summary of Significant Accounting Policies (Continued)**

**i. Proprietary Funds Revenue and Expense Classification**

In the proprietary fund's Statement of Revenues, Expenses, and Changes in Fund Net Position – Modified Cash Basis, revenues and expenses are classified in a manner consistent with how they are classified in the Statement of Cash Flows – Modified Cash Basis. That is, transactions for which related cash flows are reported as capital and related financing activities, noncapital financing activities, or investing activities are not reported as components of operating revenues or expenses.

**j. Inventory**

Inventory in the enterprise fund, acquired for resale, is valued at the lower of cost or market on the weighted average cost basis. Inventory in the general fund for chip inventory is valued at the lower of cost or market on the weighted average cost basis.

**k. Cash and Cash Equivalents**

For the purpose of financial reporting, cash and cash equivalents includes all unrestricted and restricted demand and savings accounts and certificates of deposit with a term to maturity at date of acquisition of three months or less.

The City pools the cash resources of its funds for cash management purposes. The proprietary funds essentially have access to the entire amount of their cash resources on demand. Accordingly, each proprietary fund's equity in the cash management pool is considered to be cash and cash equivalents for the purpose of the Statement of Cash Flows – Modified Cash Basis.

**l. Equity Classifications**

Government-wide Financial Statements:

Equity is classified as net position and is displayed in three components, as follows:

1. Net Investment in Capital Assets – Consists of capital assets, including restricted capital assets, net of accumulated depreciation (if applicable) and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
2. Restricted Net Position – Consists of net position with constraints placed on their use either by (a) external groups such as creditors, grantors, contributors, or laws and regulations of other governments; or (b) law through constitutional provisions or enabling legislation.
3. Unrestricted Net Position – All other net position that do not meet the definition of restricted or invested in capital assets, net of related debt.

Fund Financial Statements:

The City classifies governmental fund balance as follows:

1. Nonspendable – includes fund balance amounts that cannot be spent either because it is not in spendable form or because of legal or contractual constraints.



**CITY OF FAITH**

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
DECEMBER 31, 2013**

**(1) Summary of Significant Accounting Policies (Concluded)**

**I. Equity Classifications (Continued)**

Fund Financial Statements (Continued):

2. Restricted – includes fund balance amounts that are constrained for specific purposes which are externally imposed by providers, such as creditors or amounts constrained due to constitutional provisions or enabling legislation.
3. Committed – includes fund balance amounts that are constrained for specific purposes that are internally imposed by the government through formal action of the City Council and does not lapse at year-end.
4. Assigned – includes fund balance amounts that are intended to be used for specific purposes that are neither considered restricted or committed. Fund balance may be assigned by the City Council, Mayor, or Finance Officer.
5. Unassigned – includes positive fund balance within the General Fund which has not been classified within the above-mentioned categories and negative fund balances in other governmental funds.

Proprietary fund equity is classified the same as in the government-wide financial statements.

The City uses restricted amounts first when both restricted and unrestricted net position or fund balances are available unless there are legal documents/contracts that prohibit doing this, such as a grant agreement requiring dollar-for-dollar spending. Additionally, the City would first use committed, then assigned, and lastly unassigned amounts of unrestricted fund balance when expenditures are made.

The City does not have a formal minimum fund balance policy.

**(2) Deposits and Investments**

The City follows the practice of aggregating the cash assets of various funds to maximize cash management efficiency and returns. Various restrictions on deposits and investments are imposed by statutes. These restrictions are summarized below:

Deposits – The Municipality's cash deposits are made in qualified public depositories as defined by SDCL 4-6A-1, 9-22-6, 9-22-6.1 and 9-22-6.2, and may be in the form of demand or time deposits. Qualified depositories are required by SDCL 4-6A-3 to maintain at all times, segregated from their other assets, eligible collateral having a value equal to at least 100 percent of the public deposit accounts which exceed deposit insurance such as the FDIC and NCUA. In lieu of pledging eligible securities, a qualified public depository may furnish irrevocable standby letters of credit issued by federal home loan banks accompanied by written evidence of that bank's public debt rating which may not be less than "AA" or a qualified public depository may furnish a corporate surety bond of a corporation authorized to do business in South Dakota.

**CITY OF FAITH**

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
DECEMBER 31, 2013**

**(2) Deposits and Investments (Continued)**

Investments – In general, SDCL 4-5-6 permits Municipality funds to be invested only in (a) securities of the United States and securities guaranteed by the United States Government either directly or indirectly; or (b) repurchase agreements fully collateralized by securities described in (a) above; or in shares of an open-end, no-load fund administered by an investment company whose investments are in securities described in (a) above and repurchase agreements described in (b) above. Also, SDCL 4-5-9 requires investments to be in the physical custody of the political subdivision or may be deposited in a safekeeping account with any bank or trust company designated by the political subdivision as its fiscal agent.

As of December 31, 2013, the City's cash and investments consisted of checking and savings accounts, and certificates of deposit. All of these accounts are insured or collateralized in the City's name.

State law allows income from deposits and investments to be credited to either the General Fund or the fund making the investment. The City's policy is to credit all income from deposits and investments to the General Fund. GAAP, on the other hand, requires income from deposits and investments to be reported in the fund whose assets generated that income except where legal or contractual requirements require investment income to be credited to a fund other than the one associated with the assets. Where the governing board has discretion to credit investment income to a fund other than the fund that provided the resources for investment, a transfer to the designated fund is reported. Accordingly, in the fund financial statements, interfund transfers of investment earnings are reported, while in the government-wide financial statements, they have been eliminated, except for the net amounts transferred between governmental activities and business-type activities.

*Interest Rate Risk:* The City does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses from increasing interest rates.

*Credit Risk:* State law limits eligible investments for the City as discussed above. The City has no investment policy that would further limit its investment choices.

*Custodial Credit Risk:* This is the risk that in the event of a deposit failure, the City's deposits may not be returned to it. The City does not have a deposit policy for custodial credit risk. As of December 31, 2013, none of the City's deposits were exposed to custodial credit risk.

*Concentration of Credit Risk:* The City's places no limits on the amount that may be invested in any one issuer.

**(3) Property Taxes**

The City does not levy property taxes.



CITY OF FAITH

NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
DECEMBER 31, 2013

(4) Changes in Capital Assets

A summary of changes in governmental activities capital assets for the year ending December 31, 2013, is as follows:

	Balance 12/31/2012	Additions	Transfers/ Deletions	Balance 12/31/2013
<i>Governmental Activities:</i>				
Capital Assets, not being Depreciated:				
Land	\$			
Construction Work in Progress*				
<b>Total Capital Assets, not being Depreciated</b>				
Capital Assets, being Depreciated:				
Buildings				
Improvements Other Than Buildings				
Machinery and Equipment				
<b>Total Capital Assets Being Depreciated</b>				
Less Accumulated Depreciation for:				
Buildings				
Improvements Other Than Buildings				
Machinery and Equipment				
<b>Total Accumulated Depreciation</b>				
<b>Total Governmental Activities Capital Assets, being Depreciated, Net</b>				
<b>Total Governmental Capital Assets, Net</b>	\$			

\* Construction in Progress at December 31, 2013 is composed of engineering costs for a land acquisition, wild land fence, and runway safety area grading project for the Faith Airport, which upon completion will total approximately [REDACTED]. The City was granted a [REDACTED] federal grant for this project, to be received in 2014. Expenditures in excess of the Federal grant will be paid with the General Fund's balance.

Depreciation expense for governmental activities was charged to functions as follows:

[REDACTED]	
[REDACTED]	
[REDACTED]	
[REDACTED]	
[REDACTED]	
<b>Total Depreciation Expense - Governmental</b>	\$

CITY OF FAITH

NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
DECEMBER 31, 2013

(4) Changes in Capital Assets (Continued)

A summary of changes in business-type activities capital assets for the year ended December 31, 2013 is as follows:

	Balance 12/31/2012	Additions	Transfers/ Deletions	Balance 12/31/2013
<i>Business-Type Activities:</i>				
Capital Assets, not being Depreciated:				
Land	\$			
<b>Total Capital Assets, not being Depreciated</b>				
Capital Assets, being Depreciated:				
Buildings				
Improvements Other Than Buildings				
Machinery and Equipment				
<b>Total Capital Assets Being Depreciated</b>				
Less Accumulated Depreciation for:				
Buildings				
Improvements Other Than Buildings				
Machinery and Equipment				
<b>Total Accumulated Depreciation</b>				
<b>Total Business-Type Activities Capital Assets, being Depreciated, Net</b>				
<b>Total Business-Type Capital Assets, Net</b>	\$			

Depreciation expense for business-type activities was charged to functions as follows:

<i>Business-Type Activities:</i>	
Telephone	\$
<b>Total Depreciation Expense - Business-Type</b>	\$

CITY OF FAITH

NOTES TO FINANCIAL STATEMENTS (CONTINUED)  
DECEMBER 31, 2013

(5) Long-Term Debt

A summary of the changes in long-term debt for the years ending December 31, 2013, is as follows:

	Balance 12/31/2012	Additions	Deletions	Balance 12/31/2013	Due Within One Year
<b>Primary Government:</b>					
<b>Governmental Activities:</b>					
Capital Acquisition Leases	\$				
<b>Total Governmental Activities</b>					
<b>Total Primary Government</b>	\$				

The principal amount, above, was included in the appropriate classification of capital assets, and is being depreciated over the estimated useful-life of the asset. The asset as of December 31, 2013 is [REDACTED] with [REDACTED] in accumulated depreciation for a net book value of [REDACTED].

Debt payable at December 31, 2013, is comprised of the following:

*Capital Acquisition Lease*

Capital Lease for recreation center that bears interest at [REDACTED] percent with semi-annual payments of [REDACTED] matures January 2017 at which time the full balance is due. Financed through the General Fund.

\$ [REDACTED]

The annual requirements to amortize long-term debt outstanding as of December 31, 2013, are as follows:

	Capital Acquisition Lease	
	Interest	Principal
2014	\$ [REDACTED]	[REDACTED]
2015	[REDACTED]	[REDACTED]
2016	[REDACTED]	[REDACTED]
2017	[REDACTED]	[REDACTED]
<b>Total</b>	\$ [REDACTED]	[REDACTED]

Interest cost paid and charged to interest expense in the current period totaled [REDACTED]



**CITY OF FAITH**

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2013**

**(6) Operating Leases**

During the year ended December 31, 2003, the City began subleasing a portion of the community center to the Faith School District. This is a fifteen year operating lease that requires annual lease payments of [REDACTED]. Sublease rental income was [REDACTED] for the year ended December 31, 2013. Future rental revenues expected under this lease are as follows as of December 31, 2013:

2014	\$	[REDACTED]
2015		[REDACTED]
2016		[REDACTED]
2017		[REDACTED]
2018		[REDACTED]

The City has a lease agreement with [REDACTED] for host and remote switching services, through 2015. The lease requires minimum monthly charges of [REDACTED] plus variable fees based on service levels. Lease payments were [REDACTED] for the year ended December 31, 2013. Future minimum lease payments are as follows as of December 31, 2013:

2014	\$	[REDACTED]
2015		[REDACTED]

**(7) Retirement Plan – South Dakota Retirement System**

All employees, except for part-time employees, participate in the South Dakota Retirement System (SDRS), a cost-sharing multiple employer public employee retirement system established to provide retirement benefits for employees of the State of South Dakota and its political subdivisions. The SDRS provides retirement, disability, and survivors' benefits. The right to receive retirement benefits vests after three years of credited service. Authority for establishing, administering and amending plan provisions are found in South Dakota Codified Law 3-12. The SDRS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the SDRS, P.O. Box 1098, Pierre, SD 57501-1098 or by calling (605) 773-3731.

General employees are required by state statute to contribute [REDACTED] percent of their salary to the plan, while public safety and judicial employees contribute [REDACTED] and [REDACTED] percent, respectively. State statute also requires the employer to contribute an amount equal to the employee's contribution. State statute also requires the employer to make an additional contribution in the amount of [REDACTED] percent for any compensation exceeding the maximum taxable amount for social security for general employees only. The City's share of contributions to the SDRS for the fiscal years ended December 31, 2013, 2012, and 2011 were [REDACTED], [REDACTED], and [REDACTED] respectively, equal to the required contributions each year.

# CITY OF FAITH

## NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2013

### (8) Joint Ventures

The City participates in the South Dakota Network, Inc. (the Network), a network formed for the purpose of receiving and delivering phone traffic for its members. For the year ended December 31, 2013, the City's interest in the voting and non-voting common stock is [REDACTED] which is recorded as an investment (using the cost method) within the telephone fund. The stock will be maintained by the City as long as it participates in the Network.

Ownership in the Network consists of [REDACTED] entities, none of which have significant ownership percentages. The City has less than [REDACTED] percent ownership. Separate financial statements for this joint venture are available from South Dakota Network, Inc., Sioux Falls, South Dakota.

At December 31, 2013, this joint venture had total equity of [REDACTED] (unaudited), total liabilities of [REDACTED] (unaudited), and total assets of [REDACTED] (unaudited).

### (9) Risk Management

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During the year ended December 31, 2013, the City managed its risks as follows:

#### Employee Health Insurance:

The City purchases health insurance for its employees from a commercial insurance carrier. Settled claims resulting from these risks have not exceeded the liability coverage during the past three years.

#### Liability Insurance:

The City purchases property and liability insurance for risks related to torts; theft or damage to property; and errors and omissions of public officials from a commercial insurance carrier. Settled claims resulting from these risks have not exceeded the liability coverage during the past three years.

#### Worker's Compensation:

The City joined the South Dakota Municipal League Worker's Compensation Fund (the Fund), a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The objective of the Fund is to formulate, develop, and administer, on behalf of the member organizations, a program of worker's compensation coverage, to obtain lower costs for that coverage, and to develop a comprehensive loss control program. The City's responsibility is to initiate and maintain a safety program to give its employees safe and sanitary working conditions and to promptly report to and cooperate with the Fund to resolve any worker's compensation claims. The City pays an annual premium to the Fund to provide worker's compensation coverage for its employees. Coverage limits are set by state statute. The Fund pays the first [REDACTED] of any claim per individual. The Fund has reinsurance, which covers up to statutory limits in addition to a separate combined employer liability limit of [REDACTED] per incident. The City does not carry additional insurance to cover claims in excess of the upper limit. Settled claims resulting from these risks have not exceeded the liability coverage during the past three years.

#### Unemployment Benefits:

The City has elected to be a noncontributing member of the Unemployment Compensation Fund established by state law and managed by the State of South Dakota. As a result, the City retains all risks for liabilities resulting from claims for unemployment benefits. Claims filed and paid for unemployment benefits were [REDACTED] the year ended December 31, 2013. It is not anticipated that any additional claims for unemployment benefits will be filed in the next year.

CITY OF FAITH

NOTES TO FINANCIAL STATEMENTS (CONCLUDED)  
DECEMBER 31, 2013

(10) Emerging Accounting Standards

In June 2012, GASB issued Statement Nos. 67 and 68. Statement No. 67, *Financial Reporting for Pension Plans*, and Statement No. 68, *Accounting and Reporting for Pensions*, replace the requirements of Statement No. 50, *Pension Disclosures* and will require additional note disclosures for the City's cost-sharing multiple employer, defined benefit pension plan. These statements relate to accounting and financial reporting issues and how pension costs and obligations are measured and reported in audited financial statements. The standards describe the change from the funding-based approach to an accounting-based approach in order to improve pension information and increase the transparency, consistency, and comparability of pension information across governments.

The City will recognize its share of a collective net position liability, as well as pension expense and deferred outflows or inflows of resources for its proportionate share. Within the governmental fund financial statements, pension expenditures should be recognized equal to the total of (1) amounts paid by the City to a pension plan and (2) the change between the beginning and ending balances of amounts normally expected to be liquidated with expendable available financial resources. Note disclosures will include descriptive information about the plan and its terms, contribution rates and how they are determined, and amounts attributed to employee service and forfeitures in the current period.

The guidance related to the new standards is effective for the City's year ending December 31, 2014 for GASB 67 and December 31, 2015 for GASB 68. The City will be evaluating the impact the standards will have on the financial statements.



REDACTED - FOR PUBLIC INSPECTION

SUPPLEMENTARY INFORMATION

CITY OF FAITH

BUDGETARY COMPARISON SCHEDULE  
GENERAL FUND - BUDGETARY BASIS  
FOR THE YEAR ENDED DECEMBER 31, 2013

		Original Budget	Final Budget	Actual - Budgetary Basis	Variance
<b>Revenue:</b>					
	<i>Taxes:</i>				
313	Sales Taxes	\$			
314	Gross Receipts Business Taxes				
315	Amusement Taxes				
320	Licenses and Permits				
	<i>Intergovernmental Revenue:</i>				
331	Federal Grant				
334	State Grant				
335	Port of Entry				
335.02	Motor Vehicle Commercial Prorate				
335.03	██████ Tax Reversion				
335.04	████████████████████				
335.08	Local Government Highway and Bridge Fund				
338.01	██████████████████				
338.99	Other				
	<i>Charges for Goods and Services:</i>				
341	General Government				
342	██████████				
343	██████████████████				
346	██████████████████				
347	██████████				
348	██████████				
349	Other				
	<i>Miscellaneous Revenue:</i>				
361	Investment Earnings				
362	Rentals				
367	Contributions and Donations From Private Sources				
369	Other				
<b>Total Revenue</b>					

CITY OF FAITH

**BUDGETARY COMPARISON SCHEDULE (CONTINUED)**  
**GENERAL FUND - BUDGETARY BASIS**  
**FOR THE YEAR ENDED DECEMBER 31, 2013**

		Original Budget	Final Budget	Actual - Budgetary Basis	Variance
<b>Expenditures:</b>					
	<i>General Government:</i>				
411	Legislative				
411.5	Contingency				
	Amount Transferred				
412	Executive				
413	Elections				
414	Financial Administration				
419	Other				
	:				
421					
422					
	:				
431					
435					
437					
	:				
441					
446					
451					
452					
454					
455					
	:				
465					
465.3					
466					
470	Debt Service				
<b>Total Expenditures</b>					
391.1	Transfers In				
391.4	Compensation for Loss or Damage to Capital Assets				
<b>Total Other Financing Sources</b>					
<b>Net Change in Fund Balance</b>					
Fund Balance, December 31, 2012					
<b>Fund Balance, December 31, 2013</b>		\$			

The accompanying notes are an integral part of this statement.



**CITY OF FAITH**

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION  
DECEMBER 31, 2013**

**(1) Budgets and Budgetary Accounting**

The City follows these procedures in establishing the budgetary data reflected in the financial statements:

1. At the first regular board meeting in September of each year, or within ten days thereafter, the governing board introduces the annual appropriation ordinance for the ensuing fiscal year.
2. After adoption by the governing board, the operating budget is legally binding and actual disbursements for each purpose cannot exceed the amounts budgeted, except as indicated in item number 4.
3. A line item for contingencies may be included in the annual budget. Such a line item may not exceed [REDACTED] percent of the total municipal budget and may be transferred by resolution of the governing board to any other budget category that is deemed insufficient during the year.
4. If it is determined during the year that sufficient amounts have not been budgeted, state statute allows the adoption of supplemental budgets.
5. Unexpended appropriations lapse at year-end unless encumbered by resolution of the governing board.
6. The City did not encumber any amounts at December 31, 2013.
7. Formal budgetary integration is employed as a management control device during the year for the general fund, special revenue funds, capital projects funds, and debt service funds.

**(2) GAAP Budgetary Accounting Basis Differences**

The financial statements prepared in conformity with the modified cash basis of accounting present capital outlay expenditure information in a separate category of expenditures. Under the budgetary basis of accounting, capital outlay expenditures are reported within the function to which they relate. For example, the purchase of a [REDACTED] [REDACTED] would be reported as a capital outlay expenditure on the Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balances – Modified Cash Basis, however in the Budgetary Required Supplementary Information Schedule, the purchase of a [REDACTED] would be reported as an expenditure of the [REDACTED] [REDACTED] function of government, along with all other current [REDACTED] related expenditures.

REDACTED - FOR PUBLIC INSPECTION

OTHER REPORTS



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### INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

City Council  
City of Faith  
Faith, South Dakota

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, and each major fund of the **CITY OF FAITH** (the City) as of and for the year ended December 31, 2013, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated July 16, 2014. Our report was modified for the physical chip inventory at December 31, 2012.

#### **Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the City's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Auditor's Comments and Closing Conference, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the City's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies described in the accompanying Auditor's Comments and Closing Conference as 2013-001 and 2013-002 to be material weaknesses.

*A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying Auditor's Comments and Closing Conference as 2013-003 to be a significant deficiency.

In addition, we have another comment and suggestion for your consideration that is described in the accompanying Auditor's Comments and Closing Conference as 2013-004. This matter is offered as a constructive suggestion for the consideration of management as part of the ongoing process of modifying and improving financial and administrative practices and procedures.



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City Council  
Page Two

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the City's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance that is required to be reported under *Government Auditing Standards* and which is described in the accompanying Auditor's Comments and Closing Conference as 2013-003.

**City's Response to Findings**

The City's responses to the findings identified in our audit are described in the accompanying Auditor's Comments and Closing Conference. The City's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the responses.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the City's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. As required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.



KETEL THORSTENSON, LLP  
Certified Public Accountants

July 16, 2014

**CITY OF FAITH**

**AUDITOR'S COMMENTS AND CLOSING CONFERENCE  
FOR THE YEAR ENDED DECEMBER 31, 2013**

**A. Status of Prior Audit Findings and Recommendations**

<u>Prior Year</u>	<u>Description</u>	<u>Current Year</u>
2012-1	Financial Statement Preparation	Substantially Repeated as 2013-001
2012-2	Segregation of Duties	Substantially Repeated as 2013-002
2012-3	Approval of Disbursements	Resolved and Not Repeated

**CITY OF FAITH**

**AUDITOR'S COMMENTS AND CLOSING CONFERENCE (CONTINUED)  
FOR THE YEAR ENDED DECEMBER 31, 2013**

**B. Current Year Audit Findings and Recommendations**

**MATERIAL WEAKNESSES**

2013-001 FINDING: Financial Statement Preparation and Year End Adjustments

**Condition and Cause:** As in prior years, we were requested to draft the audited financial statements and related footnote disclosures as part of our regular audit services. During this process, we proposed a material audit adjustment to record construction in progress and reclassify an expense between funds. Ultimately, it is management's responsibility to provide for the preparation of the City's statements and footnotes, and the responsibility of the auditor to determine the fairness of presentation of those statements. From a practical standpoint, we do both for the City at the same time in connection with our audit. This is not unusual for us to do with municipalities of your size.

**Criteria and Effect:** Adjustments noted above would not have been identified as a result of the City's existing internal controls. These deficiencies could result in material misstatements to the financial statements that would not have been prevented or detected by the City's management.

**Recommendation:** We recommend management review expense accounts to ensure transactions are recorded within the appropriate fund and construction in progress is recorded. As in prior years, we have instructed management to review a draft of the auditor prepared financial statements in detail for their accuracy; we have answered any questions they might have, and have encouraged research of any accounting guidance in connection with the adequacy and appropriateness of classification and disclosure in the City's statements. We are satisfied that the appropriate steps have been taken to provide the City with the completed financial statements. It is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

**Response/Corrective Action Plan:** The City will review expenses for proper fund recording and for construction transactions. The City evaluates its risk associated with this condition on an annual basis. The Finance Officer, Debbie Brown, is responsible for this corrective action plan.

2013-002 FINDING: Segregation of Duties

**Condition and Cause:** The City has a general lack of segregation of duties in the finance office, more specifically:

- a. All finance personnel have access to the general ledger, open mail, receive unopened bank statements, and mail the signed checks.
- b. The Finance Officer and Deputy Finance Officer receive customer payments, have access to write-off and adjust customer accounts, and the customer adjustments or write-off reports are not reviewed. In addition, the Finance Officer prepares the revenue portion of the financial statements given to the City Council for review. The Finance Officer is preparing a listing of adjustments, but the listing is not currently being reviewed by someone other than herself.
- c. There is lack of controls at the [REDACTED]. The [REDACTED] orders inventory, receives inventory, and performs quarterly spot-check inventory counts. During the current year, the count documentation was reviewed by the Finance Officer for reasonableness and accuracy. Margin analysis on the [REDACTED] inventory, [REDACTED] sales and operating agreements was not performed periodically throughout the year.
- d. The [REDACTED] maintains signed checks (with one signature) on hand for larger [REDACTED]. The risk of misappropriation is mitigated by the Finance Officer's review of the bank statement, including images of cancelled checks.



**CITY OF FAITH**

**AUDITOR'S COMMENTS AND CLOSING CONFERENCE (CONTINUED)  
FOR THE YEAR ENDED DECEMBER 31, 2013**

**B. Current Year Audit Findings and Recommendations (Continued)**

**MATERIAL WEAKNESSES (Continued)**

2013-002 FINDING: Segregation of Duties (Continued)

Criteria and Effect: Internal controls should be in place to provide reasonable assurance that all financial transactions are reviewed and approved before payments are made and reports are generated. Controls also need to be in place to ensure all revenue is processed and recorded correctly. Proper segregation of duties and functions assures adequate control over safeguarding of assets and the reliability of financial records and reporting. The effectiveness of the internal control system relies on enforcement by management.

Recommendations:

- a. The overall lack of segregation of duties over the disbursement process is due to the limited number of accounting personnel, which is typical in a city of this size. However, the risk of misappropriation is mitigated by the Mayor reviewing the unopened bank statement.
- b. The listing of account adjustments and write-offs from the accounting software should be reviewed monthly by a City Council Member.
- c. The Finance Officer should continue to review the periodic inventory count paperwork and perform random count checks. Additionally, margin analysis (direct cost of sales as a percentage of sales) should be performed at least monthly by the Finance Officer and reviewed for reasonableness based on gross margin percentages of [REDACTED], [REDACTED] and operating agreements. The results should be reviewed with a City Council member.
- d. Signed checks should not be maintained on hand, as it creates the potential for misappropriation of cash. As noted above, the risk is mitigated by the Finance Officer's review of the bank statement, including images of cancelled checks.

Response/Corrective Action Plan: The City attempts to maintain proper segregation of duties with the staff available. The Finance Officer, Debbie Brown, is responsible for this corrective action plan.

**SIGNIFICANT DEFICIENCY**

2013-003 FINDING: Budgetary Overdrafts

Condition: The City had budgetary overdrafts of [REDACTED] in the [REDACTED] and [REDACTED] in [REDACTED] and [REDACTED], of the General Fund during the year ended December 31, 2013.

Criteria and Effect: Budgetary overdrafts are a violation of South Dakota Codified Law 9-21-9.

Recommendation: The City in the future should complete supplemental appropriations for unbudgeted expenditures, and complete transfers to cover each fund's expenses.

Response/Corrective Action Plan: The City makes every effort to supplement the budget when needed and will continue to be more diligent in this process. The Finance Officer, Debbie Brown, is responsible for this corrective action plan.